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MINISTRY OF COMMERCE AND INDUSTRY

RESOLUTION

New Delhi, the 3rd October, 1955

No. C.I. 24(18)/55.—By a resolution No. 3-T(3)/52, dated the 30th October, 1952, the Government of India requested the Tariff Commission to make an enquiry into the prices of rubber tyres and tubes manufactured by the tyre companies in India and to submit its recommendations regarding fair prices. The Commission submitted its Report at the end of June, 1955. The main conclusions and recommendations of the Commission are briefly summarised below:—

(i) If the excise duty continues to be charged on the existing basis, namely, the list price less discount of 10 per cent., a uniform reduction of 11 per cent. should be made in the current net dealer prices and list prices. If the basis of charging the excise duty is revised, as requested by the tyre companies so as to take into account the year-end discount of 2½ per cent., in addition to 10 per cent., the net dealer prices and list prices should be reduced by 11·56 per cent. The fair prices so arrived at should remain in force till 31st December, 1957, subject to a formula suggested by the Commission for adjustment on account of variations in the cost of raw rubber, fabric and carbon black.

(ii) No reduction should be made in the existing rates of discounts on replacement sales, except with the approval of Government.

(iii) Prices for original equipment and Government should continue to be fixed by negotiations as at present. No control need be exercised over export prices.

(iv) Taking into account the two price reductions effected by the tyre companies since October 1952 when the Commission was asked to take up this enquiry the fair prices recommended will be lower than the prices prevailing in October 1952 by 17·6 per cent. in the case of passenger car tyres and tubes and 19·7 per cent. in the case of other tyres and tubes, if the excise duty continues to be charged on the existing basis and the current prices are accordingly reduced by 11 per cent., and by 18·1 per cent. in the case of passenger car tyres and tubes and 20·3 per cent. in the case of other tyres and tubes, if the basis of charging the excise duty is revised as requested by the tyre companies and the current prices are accordingly reduced by 11·56 per cent.

2. The Commission has based the above recommendations on an analysis of the cost of production of tyre companies and their over-all trading results since 1946. The principal facts which have emerged from the Commission's enquiry are the following:—

(i) While the price of rubber was controlled, the benefit to the consumer was nullified by increases in other elements of cost. The two elements of cost in which there were the most remarkable increases were—

(a) factory overheads; and

(b) selling and distribution expenses.

Those two elements of cost were clearly susceptible of control by the tyre companies. The increase of 85 per cent. between 1946 and 1953 in factory overheads in the case of the two manufacturing companies was excessive, having regard to the actual increases in their output. Likewise, the selling and the distribution expenses went up over the same period by 104 per cent. in the case of one manufacturer and 229 per cent. in the case of the other. The increase in the case of the two firms who get their tyres manufactured by Dunlops and do their own marketing were 127 per cent. and 215 per cent. respectively.

(ii) While no serious efforts were made to check an increase in the cost of manufacture, the selling prices fixed by the tyre companies were such that they earned unduly high profits. The ratio of gross profits to capital employed varied, according to the Commission, from 19 per cent. to 37 per cent. in the case of Dunlops between 1946 and 1953, and from 47 per cent. to 77 per cent. in the case of Firestone between 1946-47 to 1952-53. The Commission, after examining the cost figures, has concluded that throughout the years 1946 to 1953 the actual prices of tyres and tubes were in excess of the fair prices as determined by the Commission by amounts which varied from 21·79 per cent. to 6·88 per cent.

(iii) The Governmental assistance given to the tyre companies during the war did not have any effect on their costs after 1945 and there is no reason to believe that during the period under review the tyre companies continued to receive any special benefits or concessions from Government which they did not pass on to the consumer.

3. In the light of the above findings the Commission has recommended a strict control over selling prices of tyres and tubes on the following ground:—

> "The complete elimination of price competition results in excessive reliance being placed on publicity, personal liaison and service attractions of various sorts leading to a competative increase in selling and distribution expenses. While price competition benefits the consumer, the kind of competition which prevails among the tyre companies leads to a growing burden being placed on the consumer. Government should, therefore, exercise strict control over the selling and distribution expenses incurred by the tyre companies".

4. Copies of the Commission's report were sent to the Companies concerned, *viz.*, Dunlop Rubber Co. (India) Ltd., Firestone Tyre & Rubber Co. of India Ltd., Goodyear Tyre & Rubber Co. (I) Ltd., and the Indian Tyre & Rubber Co. (India) Ltd., As, for reasons explained in the Report, the Commission took Dunlops as the representative unit for the purpose of determining a representative fair price, the main criticisms against the Commission's recommendations have been made by Dunlops. The more important of these are examined below.

5. In recommending a reduction in the current net dealer prices and list prices, the Commission has discussed the policy of tyre companies in regard to the disposition of their profits in the past. Dunlops which had an initial paid-up capital of Rs. 50 lakhs gave bonus shares from out of profits to the extent of Rs. 110 lakhs, thus raising the capital to Rs. 160 lakhs. The capital dividend ratio has not been considered in the case of the other tyre companies because their capital is small or nominal. The capital of Firestones is Rs. 20,000/-, of Goodyears Rs. 15,000/- and of Indian Rubber Company Rs. 7 lakhs plus Rs. 7 lakhs bonus shares. These companies remit their profits to the parent companies from whom also they get their finances. In discussing the return on the capital employed by Dunlops the Commission has observed as follows:—

> "In calculating fair profits we do not consider it proper to take into account the additional liability incurred by the company by issuing bonus shares. At the same time, in view of the importance of technology and research in the case of this industry and its dependence on foreign organisations for this purpose, we consider it fair to reckon the dividend due to the ordinary shareholders at 10 per cent. tax free" on the original amount of Rs. 50 lakhs.

6. The above observation has given rise to the impression that the Tariff Commission is of the view that the shareholders of a company whose reserves have been capitalised by the issue of bonus shares are not entitled to a return on those shares. This is the main issue of principle on which Dunlops have based their criticisms. Any such impression, however, is based on a misconception of the views of the Commission. In a letter addressed to Government, the Chairman has pointed out that the Commission has nowhere stated that future dividends should not exceed 10 per cent. on the original capital. In fact the Commission is of the view that the industry

should retain larger amounts in the business than declare high dividends; and a larger share of the profits would not be retained in business unless what is reinvested also earns a return in the same way as the original capital. But the proportion of profits ploughed back into the industry has little relevance in determining whether the profits themselves were fair or too high. It was in the context of assessing whether the prices charged were excessive that the Commission took into account only the original capital, which was actually invested in the industry at the beginning of the period under enquiry. This does not mean that such portion of the capital as is ploughed back in the form of bonus shares should not qualifiy for dividend equally with the historical capital.

7. The Commission considers that the administrative selling and distribution expenses should be brought down to the level at which they stood in 1953. If this were done, the Dunlop Co. would not only be able to declare a dividend of 10 per cent. on its total share capital—original as well as bonus shares—but it will also be able to put by adequate sums in reserve. The amount should cover that portion of finance for its normal development programme over the next few years which should legitimately come from internal sources.

8. In the circumstances stated above, Government are of the view that the main objection of Dunlops to the reduction in prices is not tenable.

9. The tyre companies have also pleaded that bonus to employees should not come out of profits but should be treated as an element of costs because although they are often referred to as a profit-sharing bonus, in actual fact the industry has to pay it regardless of the quantum of its profits. Further, the tyre companies have requested that they should be allowed depreciation on the basis of three shift working, while the Commission has allowed it only on double shift working. Government have considered these points. The procedure followed by the Commission in the matter of bonus is in keeping with the line followed for other industries. In any event the inclusion of bonus as an element of cost would change the figure of gross profits and not affect the recommendation of the Commission regarding the fairness of the net profits earned by the industry and the recommendations regarding prices. As regards depreciation, it is a fact that this industry works three shifts. On the other hand, depreciation is made up of a number of elements and while depreciation due wholly to the wear and tear of machinery is doubled with two shift working and trebled with three shift working, other elements do not increase in the same proportion. Therefore, by allowing depreciation on two shift basis while the factory works on a three shift basis, no real injustice is being done to the tyre companies.

10. The Government have, therefore, decided that the tyre companies should revise their prices in accordance with the formula for fair prices for rubber tyres and tubes recommended by the Commission, with suitable adjustments to take into account the recent increase in the price of raw rubber. The Tyre Companies have been called upon to issue a revised price list with effect from the 10th October, 1955.

11. The Commission has also made the following ancillary recommendations:—

(a) Government should explore the possibility of securing imports of tyres and tubes with a view to providing some measure of competition to the Indian companies.

(b) (i) A pilot project should be started for manufacture of tyres and tubes and (ii) special assistance should be offered to Indian enterprises wishing to enter this field, either independently or in collaboration on reasonable terms with foreign enterprises.

(c) Government should examine the desirability of securing larger participation of Indian capital in the tyre companies operating in India in order that the benefit accruing to the national economy from the manufacture of tyres and tubes may be enhanced through the retention in the country of a larger proportion of the profits earned in this business.

These recommendations are being examined by Government.

H. V. R. IENGAR, Secy.

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